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Chapter 4: Corporations

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CHAPTER 4

Corporations

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§4.1. Introduction. During the 1969 SURVEY year many significant changes in the Massachusetts business corporation law were enacted under Chapter 392 of the Acts of 1969. This chapter will describe the principal changes made by this act, and other legislative developments in the corporations area.

§4.2. Incorporation. The mechanics of incorporation have been completely streamlined by the amendments to Section 12 of Chapter 156B.[1] Now one person may, without a meeting, merely sign the articles of organization form and file it with the secretary of the Commonwealth. Whereas Section 12 previously required three or more *natural* persons as incorporators of a corporation, it has been amended so as to provide that one or more persons may act as incorporators. Furthermore, an incorporator need no longer be a natural person; it may be another corporation[2] or some other form of business organization.

An amendment to Section 12 also permits action to be taken by the incorporator or incorporators without a meeting. This is similar to the provision of Section 43 which permits shareholders to act without meetings. The only requirement under the amended Section 12 is that all the incorporators consent to the action in writings, which are then filed with the corporate records. The consents of the incorporators need not be in the same instrument, and, in fact, may be in the articles themselves. Furthermore, the powers of incorporators have been significantly broadened. In addition to adopting the by-laws and electing the initial directors and officers, the incorporators are now specifically authorized to take any other action which might be taken by shareholders after the articles of organization have become effective.

Under the amended section, the effective date of incorporation, the day the existence of a corporation begins, may be better controlled. This date is based upon when the articles or organization become effective. Section 12 now provides that the articles shall become effective *either* when filed with the secretary of the Commonwealth or

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§4.2. [1] Acts of 1969, c. 392, §8.

[2] By an amendment to Chapter 156B, Section 9(o), a corporation is specifically authorized to act as an incorporator. Acts of 1969, c. 392, §6.

at a later date, not more than 30 days after filing, as specified in the articles.

These amendments provide greater flexibility for incorporation without significant changes in the substantive law. In one instance, however, they are not as broad in scope as the recent amendments in Delaware. Under Delaware law, incorporators are empowered to act as directors until directors are elected.[3]

§4.3. **Corporate powers.** The most significant amendment in this area was the addition of Section 9A to Chapter 156B. This section empowers a corporation to be a partner in any business enterprise which the corporation would have power to conduct by itself.[1] While enactment of such statutes has been the trend in many other states such as Delaware and New York, this concept is contrary to a basic theory of corporation law — a corporation is to manage its affairs separately and exclusively, and to be responsible to its shareholders. Allowing a partner to affect corporate activities, and thereby impinge on the powers to be exercised by the shareholders, directors and officers, was so inconsistent with the corporate nature as to be contrary to public policy or ultra vires.[2] Given the modern complexity of business combinations and the pressures of economics, however, this amendment was most essential for keeping our laws current. In order that the corporation may avoid the necessity for defensive action in the form of an amendment to the articles of organization negating any potential new liability as a partner, such right to enter into partnerships exists only where the corporation is specifically authorized to do so by its articles of organization or an amendment thereto. Prior to this amendment many corporations have acted as joint venturers upon the belief that such activity was not prohibited by law.[3] In order not to cast doubt on the validity of existing joint ventures, specific reference to joint ventures has not been included in the amendment.

Section 9(*l*), which authorizes a corporation to have pension, profit-sharing and similar types of retirement, incentive and benefit plans for its directors, officers and employees, has been amended[4] to authorize a corporation to have such plans for such persons of any other corporation, 50 percent of the outstanding voting stock of which is owned by it. This will enable, for example, a parent corporation, to use the same plan for the employees of its subsidiaries.

[3] Del. Code Ann. tit. 8, §107 (1967).

§4.3. [1] Acts of 1969, c. 392, §7.

[2] See, e.g., Whittenton Mills v. Upton, 76 Mass. 582 (1858). This general rule was often held inapplicable where the partnership agreement provided that the entire management would be entrusted to the corporation (see Bates v. Coronado Beach Co., 109 Cal. 160, 41 P. 855 (1895)) or to a joint venture (see Luhrig Collieries Co. v. Interstate Coal & Dock Co., 281 F. 265 (S.D.N.Y. 1922)).

[3] Ibid. Cf. Mechem, The Law of Joint Adventurers, 15 Minn. L. Rev. 644, 651 (1931).

[4] Acts of 1969, c. 392, §4.

The amendments in this area fell short of the liberal trend of the Delaware corporation law in one important respect. House Bill No. 1180 proposed to amend Section 13(a)(3) of Chapter 156B by adding thereto the following: ". . . it being sufficient to state, with or without reference to any specific business or purpose, that the purpose of the corporation is to engage in any lawful business permitted by this chapter." While this provision was not enacted, the need for wide-ranging purposes is obvious considering the trend toward conglomerate corporations.

§4.4. Liability and indemnification. Sections 60 through 64 of Chapter 156B provide for liability of directors, officers and incorporators to the corporation, shareholders or creditors for certain conduct such as making improper stock issues, unlawful distributions, or signing false statements or reports. Section 65, however, contains a "prudent man" rule with respect to such *statutory* liabilities, in that no director, officer, or incorporator shall be liable who has discharged his duties "in good faith and with that degree of diligence, care and skill which prudent men would ordinarily exercise under similar circumstances in a like position." Primarily because of the difficulties of proof of compliance with this standard, Section 65 has been amended[1] to specify certain objective tests which, if met, will exonerate such persons. Therefore, a director, officer or incorporator, in discharging his duties in good faith, "shall be entitled to rely upon the books of account of the corporation or upon written reports made to the corporation by any of its officers, other than such person, or by an independent public accountant."[2] It is most important to note that the reports must be *written* and that reports of any attorney are not included.

Indemnification of directors, officers, employees and agents acting in good faith is provided for in Section 67 of Chapter 156B. This section has been amended[3] to allow indemnification for expenses incurred by such persons in defending a civil or criminal action or proceeding in advance of final disposition of the action or proceeding.

With the advent of the so-called "federal" law on the liability of corporate personnel in SEC matters,[4] the subject of indemnification has received increased attention. Frequently, corporations provide indemnification if such persons are not guilty of misfeasance. This policy, however, breaks down in a situation in which one encounters difficulty proving his innocence. While he regards himself as innocent, there is always a chance that a judge or jury might find otherwise. These increasing risks imposed on corporate personnel (as well as on accountants and underwriters) have led many corporations to turn

§4.4. [1] Acts of 1969, c. 392, §16.
[2] Ibid.
[3] Acts of 1969, c. 392, §17.
[4] See, e.g., SEC v. Texas Gulf Sulphur, 401 F.2d 833 (2d Cir. 1968); Escott v. Bar Chris Construction Corp., 283 F. Supp. 643 (S.D.N.Y 1968).

increasingly to insurance as an umbrella against liability. Generally, the corporation pays for insurance to cover the risk that it may have to indemnify an officer. At the same time it takes out a companion insurance policy written to cover the individual against the possibility that he may be held liable without indemnification being applicable. These policies are sold in a package with the division of premiums between the two risks, namely, one-tenth of the premium for individual coverage and nine-tenths for the corporation coverage.

The difficulty, however, is whether it is ultra vires or otherwise improper to spend corporate funds to pay the full premium since such insurance covers situations for which there is no indemnification, and therefore, by hypothesis, situations in which the individual has not been serving the best interests of the corporation. Nevertheless, corporate personnel are now demanding fairly complete protection, and the corporation must be able to offer the same in order to attract competent personnel. Section 67 has thus been further amended[5] to authorize corporations to purchase insurance on behalf of its personnel against any liability, regardless of whether the corporation would have the power to indemnify the personnel against any liability.

§4.5. **Series stock.** Section 26 of Chapter 156B has been amended[1] to broaden the authority of directors to permit them (if authorized by the articles of organization), where the corporation has issued several series of stock of the same class, to vary the dividend characteristics between different series. Experience under Chapter 156B has indicated that, in proper cases, if the characteristics of different series in a class are to be established from time to time by the directors to meet the requirements of the financial market, it is desirable for the directors to be able to establish not only different dividend rates, as previously permitted by Chapter 156B, but also different rights as to dividends with respect to each series. By way of illustration, this amendment would permit one series to be cumulative and another, noncumulative.

§4.6. **Merger.** Under Section 78 of Chapter 156B, the vote of at least two-thirds of each class of stock of each constituent corporation, outstanding and entitled to vote on the question, is required for the approval of a merger. The only exception to this requirement in Massachusetts has been under Section 82, in the case of a merger of a subsidiary into a parent corporation owning at least 90 percent of the outstanding shares of each class of stock of the subsidiary. Under both statutes, however, there are certain appraisal rights for objecting or dissenting shareholders, except that under Section 82(e) such rights are restricted to only the objecting shareholders in the subsidiary Massachusetts corporation.

Section 78 has now been amended[1] to provide under specified condi-

[5] Acts of 1969, c. 392, §18.

§4.5. [1] Acts of 1969, c. 392, §11.

§4.6. [1] Acts of 1969, c. 392, §§19, 20.

tions another exception allowing a merger by the simplified procedure of a directors' vote and without, in specified circumstances, appraisal rights to the shareholders involved. Unless there is a contrary provision in its articles of organization, a corporation may now effectuate a merger without a vote of its shareholders provided that the agreement of merger does not change the corporation's name, the amount of authorized shares of any class of stock, or any other provisions of the articles or organization; and further provided that the directors are authorized under Section 21 of Chapter 156B to issue stock which is to be issued in the merger and that such stock does not exceed fifteen percent of the stock of the same class outstanding immediately prior to the effective date of the merger.

§4.7. Dissolution of a corporation: Deadlock. Section 99 of Chapter 156B provides for the filing of a petition for dissolution in the Supreme Judicial Court by shareholders of not less than forty percent of the outstanding shares entitled to vote thereon in two situations involving a "deadlocked" corporation. The first is where the directors are deadlocked in the management of corporate affairs, and the shareholders are unable to break the deadlock; the second is where the shareholders are deadlocked by reason of voting powers and have failed "for a period which includes at least two consecutive annual meeting dates" to elect successors to directors. Since the old Chapter 156 contained no reference to two consecutive annual meetings, and because no useful purpose is served by waiting for a second annual meeting to correct such a deadlock, Section 99 has been amended[1] to delete the quoted language from the second situation.

§4.8. Certificate of condition: Requirement of auditor. Every Massachusetts corporation is required under Section 109 of Chapter 156B to file with the secretary of state an annual report of condition. If the corporation's outstanding capital stock was $200,000 or more, Section 111 required that a sworn statement of an auditor be attached to such report. However, in determining the amount of issued stock, no par stock was treated as $100 par value stock. By the addition of a Section 109A[1] and an amendment to Section 111,[2] this rather illusory standard has been replaced by a more realistic approach. The sworn statement will now be required only if the report shows total assets of the corporation in excess of $500,000.

§4.9. Record date. Under Section 42 of Chapter 156B the directors are authorized to fix a record date for such purposes as determining stockholders who are entitled to vote or receive dividends, or at least to close the transfer books for a specified period. Section 42 created certain problems, however, in that it was silent as to what date to use when the directors failed either to fix a record date or to close the transfer

§4.7. [1] Acts of 1969, c. 392, §23.

§4.8. [1] Acts of 1969, c. 392, §25.
[2] Id. §26.

books. The amendment to Section 42[1] now establishes the rules in such cases. If no other record date is set by the directors and the transfer books are not closed, the record date for determining shareholders having the right to notice of, or to vote at, a meeting of shareholders shall be at the close of business on the day next preceding the day on which notice is given. The record date for determining shareholders for any other purpose shall be at the close of business on the day on which the directors act with respect thereto.

§4.10. Revival of dissolved corporation. The authority of the secretary of the Commonwealth under Section 108 of Chapter 156B to revive a corporation was limited to those dissolved within five years and was conditioned upon a proviso that one of the specified methods of dissolution had been used by the corporation. Section 108 has been amended[1] to permit revival without any such limitation of time and regardless of the manner in which dissolution occurred.

§4.11. Professional corporations. Section 3 of Chapter 156A, the Professional Corporations Act,[1] incorporated by reference the provisions of Chapter 156, the old business corporation law, a fact which was overlooked when the legislature enacted Chapter 156B. Section 3 has now been amended[2] to incorporate Chapter 156B rather than Chapter 156.

§4.12. Real estate conveyances. Effective January 1, 1970, by reason of an amendment to Section 8 of Chapter 155[1] and the addition of a Section 115 to Chapter 156B,[2] any recordable instrument purporting to affect an interest in real estate, executed in the name of a corporation by two of its officers — one being the president or vice-president and the other being the treasurer or assistant treasurer — shall be binding on the corporation notwithstanding any inconsistent provisions in the corporation's papers, such as the articles of organization, by-laws or resolutions.

§4.13. Proposed legislation. During the 1969 SURVEY year, considerable effort was directed toward revising Chapter 180.[1] The prin-

§4.9. [1] Acts of 1969, c. 392, §13.

§4.10. [1] Acts of 1969, c. 392, §24.

§4.11. [1] For an excellent article on the Massachusetts Professional Corporations Act, see Smith and Ault, The Corporate Professional — United States v. Empey, 54 Mass. L.Q. 14 (1969), particularly with respect to the requirement of at least three directors from the same profession. Because of the restrictive provision in Section 8 of Chapter 156A, i.e., no person "may be simultaneously an officer, director or shareholder of more than one professional corporation," it may become increasingly difficult to find persons qualified and willing to act as directors.
[2] Acts of 1969, c. 392, §29.

§4.12. [1] Acts of 1969, c. 245, §1.
[2] Id. §2.

§4.13. [1] The Chapter 180 subcommittee of the Corporate Law Committee of the

cipal purposes of this effort were (1) to simplify the mechanics of incorporation and of effecting changes in organization, such as mergers;[2] (2) to coordinate the appropriate provisions of Chapter 156B by incorporating by reference these provisions into Chapter 180, thereby completely repealing Chapters 155 and 156; and (3) to cover all "nonprofit" corporations by Chapter 180. While no legislation was enacted, the proposed revisions of Chapter 180 are laudatory and are, therefore, certainly worthy of further legislative efforts.

Boston Bar Association was the principal draftsman of House Bill No. 1181, which was not enacted in the 1969 SURVEY year.

2 At the present time, a merger of a Chapter 180 corporation requires a special act of the legislature. Under House Bill No. 1181, the merger provisions of Chapter 156B would apply.